Statement of Denise Farris on Behalf of Women Impacting Public Policy

Before The U.S. House of Representatives Committee on Small Business

"SBA's Progress in Implementing the Women's Procurement Program"

January 16, 2008

Good morning. Chair Velázquez, Ranking Member Chabot, and Members of the Committee, my name is Denise Farris. Thank you for holding this hearing and thank you for inviting me to testify. I am appearing today on behalf of Women Impacting Public Policy (WIPP) and am honored to speak on behalf of its membership which is well over half a million women business owners nationwide. I own my own law firm, Farris Law Firm LLC, located in Stilwell, Kansas.

Just to give you a little background on my practice, I am a commercial construction lawyer and for the past seventeen years I have focused on the constitutional parameters of affirmative action in government contracting. I have been a speaker and author on the topic, most recently in the American Bar Association's book, Federal Government Construction Contracts, 2003. I have represented women, minority and majority-owned firms, as well as large business organizations on this issue, and regularly serve as a consultant in the review of pending legislation from a local, county, state and federal level. I am also currently working on a multi-coalition, minority, women and non-minority initiative to implement a formal small business and affirmative action plan in the State of Kansas. I am sure the Committee can appreciate how important this proposed rule is to me both professionally and personally.

As this Committee well knows, Public Law 106-554 {Section 8(m) of the Small Business Act, 15 U.S.C. Section 637(m)} was passed in the year 2000. The law sought to address and remedy discrimination against women business owners in federal contracting by creating a women's procurement program which gives contracting officers the ability to restrict competition to women-owned businesses for up to five percent of all federal contracts. The law defined women-owned small businesses (WOSBs) that

qualify for restricted competition as small according to the SBA size standards, majority-owned by women, and certified as economically disadvantaged. The law further states that WOSBs need not be economically disadvantaged to qualify for procurement preferences in contracts up to $3 million ($5 million in manufacturing) in industries where they are found to be "substantially underrepresented." The law gave the Small Business Administration (SBA) the responsibility to determine which industries were underrepresented by women, requiring a study of the data to determine which industries were "substantially underrepresented".

Initially, the SBA undertook its own study, but rejected it internally. For seven long years, the SBA studied and restudied the data with the culmination of the report published by the RAND Corporation, titled, "The Utilization of Women-Owned Small Businesses in Federal Contracting," published in the summer of 2007.

The RAND Corporation was asked by the SBA to compute disparity ratios for WOSBs using contract dollars and number of contracts. RAND computed the disparity ratios in four different ways: (1) number of contracts using total WOSB numbers; (2) number of contracts using WOSBs registered in the Central Contractor Registration (CCR); (3) contract dollars using all WOSBs; and (4) contract dollars using WOSBs registered in the CCR. The method used to define industries was the North American Industry Classification System (NAICS) codes.

The RAND Study concluded that, depending on how SBA wanted to interpret the data, 87 percent of industries would be considered underrepresented, or 0 percent of industries would be considered underrepresented depending on whether contract dollars or number of contracts were used and whether the total number of women-owned firms

or only those registered in the CCR were used. Even the impact of whether the SBA used a 2 digit (broad category), 3 digit, or 4 digit (narrow industry category) NAICS code affected the outcome.

The SBA, in the proposed rule, chose to use the disparity ratio that analyzed the number of WOSBs registered in the CCR by contract dollars awarded, and the 4 digit NAICS code as the industry definition, thus choosing the narrowest method of data analysis. The proposed rule identifies four NAICS codes that will be subject to restricted competition: cabinetmaking, engraving, other motor vehicle dealers, and national security and international affairs; however, there is an additional requirement even for those four categories under this proposed rule—an agency must perform an internal audit of its past contracting actions to show that it is rectifying its own past discrimination before the contract can be designated for restricted competition.

WIPP believes that the practical effect of this rule is that virtually no contracts will ever be successfully set aside under this program as structured in the proposed rule.

The proposed SBA ruling that we are discussing today also carries a significant impact in that it incorrectly suggests to state and local authorities that gender based programs are subject to an incorrect legal standard of review, thus making it more difficult for gender based programs to survive at a state and local level.

Let me devote some time to discuss the legal side of this proposed rule. First, we believe that the SBA proposed rule applies the wrong legal standard of review. Second, the proposed rule not only incorrectly applies strict scrutiny, but creates a new "Strict Strict Scrutiny" standard.

On page one of the RAND Study, which forms the statistical underpinning for the SBA's current rule as described above, a detailed analysis of the Supreme Court decisions in *Croson*[1] and *Adarand*[2] makes the leap of applying the *Croson* and *Adarand* cases to gender-based studies. But in fact, each of these cases dealt specifically with legal challenge to a race-based, not gender-based, program. The Study then makes the following statement: "Although there have been few cases concerning women-owned businesses per se, it appears that Congress **assumes** that a similar standard would hold – hence its stipulation that before the SBA can restrict bidding to WOSBs [women-owned small businesses], it must first show that there are disparities that adversely affect them." No citations or other references are listed to back up this "assumption," and the conclusory statement ignores nearly forty years of Supreme Court precedent on this exact issue.

In fact, this issue was squarely addressed by the U.S. Attorney General's office. In its June 28, 1995, report to the Department of Justice General Counsels, the Assistant Attorney General, Walter Dillinger, concluded that the *Adarand* decisions, which applied a "strict scrutiny" review, did not apply to gender-based affirmative action programs. Specifically, the report concluded:

> "*Adarand* did not address the appropriate constitutional standard of review for affirmative action programs that use gender classifications as a basis for decision making. Indeed, the Supreme Court has never resolved the matter. (Footnote omitted). However, both before and after *Croson*, nearly all circuit court decisions have applied intermediate scrutiny to affirmative action measures that benefit women. (Footnote omitted). The Sixth Circuit is the only court that has

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[1] *City of Richmond v. J. A. Croson*, 488 U.S. 469 (1989).

[2] The "*Adarand" decision was issued in three separate Supreme Court decisions: Adarand Constructors, Inc. v. Pena,* 515 U.S. 200 (1995); *Adarand Constructors, Inc. v. Slater,* 528 U.S. 216 (2000); and *Adarand Constructors, Inc. v. Mineta*, 532 U.S. 967 (2001).

equated racial and gender classifications: purporting to rely on *Croson*, it held that gender-based affirmative action measures are subject to strict scrutiny. (Footnote omitted). That holding has been criticized by other courts of appeals, which have correctly pointed out that *Croson* does not speak to the appropriate standard of review for such measures." (Walter Dillinger, Assistant Attorney General, "Memorandum to General Counsels", U.S. Department of Justice, Office of Legal Counsel, Washington DC. June 28, 1995)

The significance of these different review standards is illustrated below:

Standard of Review	**Applicable**	**Criteria**	**Explanation**
Strict Scrutiny	Race National Origin Religion Alienage **(SUSPECT CLASSIFICATIONS under Equal Protection Clause of 5th and 14TH Amendment)**	Class justified via: 1. **Compelling** state interest And 2. **Narrowly tailored** program	1. Proof of past discrimination thru disparity study 2. Flexible program based on local availability / capability; not overinclusive (ie goals for non-represented groups); not underinclusive (must contain race neutral measures such as small business development, bonding, etc.) 3. Most difficult to justify on equal protection grounds.

Intermediate Scrutiny	Gender Illegitimacy	Class justified via: 1. **Important** state interest And 2. Program **substantially related** to serving that interest	1. No case law supporting disparity study requirement. Only government acknowledge-ment of important policy reason. 2. No case law restrictions as in "Strict Scrutiny" above. 3. Easier to justify on equal protection grounds.
Rational Basis	All classifications except the above	1. Class is "rationally related" to 2. Serving legitimate state interest	1. Widespread discretion to create classes 2. Easiest to justify on equal protection grounds – extremely difficult to challenge.

Accordingly, if Public Law 106-554 were subject to strict scrutiny, it would require a disparity study and a "narrowly tailored program" per the above. However, as a gender based program, it is our belief that Public Law 106-554 does not require a disparity study and could be immediately implemented with no further statistics or additional agency-by-agency investigations. We would argue that strict scrutiny is not the proper test for the SBA or the Department of Justice to assume. We believe, based on

legal history, that a gender based program should use "intermediate scrutiny" as the proper legal standard of review.

A long line of legal cases, but most importantly the 1989 decision of *City of Richmond v. J. A. Croson*, indicated that all programs based on race were inherently suspect and would only be implemented following proof of a compelling government interest, coupled with a program narrowly tailored to address that interest. This standard first applied only to local and state programs, but following the line of *Adarand* Supreme Court cases in the late 1990's, extended the standard to federal programs as well. Thus all race-based programs required a statistical disparity study to justify affirmative action programs and goals, and additionally required narrowly tailored programs to meet those goals, "narrowly tailored" being defined as flexible, regional, and ethnic group specific, containing waiver processes; and also containing race-neutral measures such as small business programs for access to capital and bonding. Although this standard applied only to race-based programs, for years gender-based programs have incorrectly been subjected to the same legal standard.

In fact, under *Craig v. Boren*, a 1976 case argued by then attorney Ruth Bader Ginsburg[3], the Supreme Court has long held that gender-based programs are subject to "intermediate scrutiny" standards, meaning that to justify the program, the government need only prove an important governmental interest, and a program substantially related to achievement of that interest or purpose. Simply put, intermediate scrutiny does not

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[3] *See e.g., Reed v. Reed*, 404 U.S. 71 (1971): First gender classification case measured under "rational basis" review; *Frontiero v. Richardson*, 411 U.S. 677 (1973); acknowledging "Our country has had a long and unfortunate history of sex discrimination".; *Craig v. Boren*, 429 U.S. 190 (1976), argued by then attorney and current Supreme Court Justice Ruth Bader Ginsburg in decision which created "intermediate scrutiny" for gender based classifications.

require disparity studies to implement the program, nor does it require the narrow structuring required in race-based programs.

In this instance, under intermediate scrutiny the SBA easily possesses the legal ability to recognize the following and act accordingly:

> 1. As of 2007, 7.7 million businesses are 51% owned and controlled by women; employing 7.1 million people and generating revenues of $1.1 trillion. [4]
> 2. Despite this fact, women-owned businesses receive only a mere 3.4% of federal procurement contracts. [5]

This differential, standing on its own, immediately implies that either the government is not doing an adequate job of reaching out to WOSBs to integrate them into the procurement system, or alternatively that there remain active barriers preventing women-owned businesses from open competition in federal procurement.

Couple this with evidence of the overall importance of women-owned businesses to the economy (again, 7.7 million women-owned businesses employing more than 7.1 million people, and generating $1.1 trillion in sales), and the intermediate scrutiny standards are met. This is proof of an important government interest --support of women-owned businesses in the national economy and all of the flow down positive effects of same - along with a program substantially related to achievement of that interest – five percent restricted set-aside to encourage procurement officers to more aggressively recruit and move WOSBs into the system, and a percent that is extremely modest given the fact that WOSBs represent 50 percent of the total businesses in the United States.

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[4] Center for Women's Business Research. http://www.cfwbr.org/facts/index.php (2007).

[5] "The Utilization of Women owned Small Businesses in Federal Contracting", Kauffman-Rand Institute for Entrepreneurship Public Policy, Ch. 1, p. 1; (2007).

The SBA not only misapplied the legal standard, in our opinion, but took it a step further and created a new "Strict Strict" scrutiny standard for gender-based programs for women.

The SBA has acknowledged disparity in only four narrow areas: cabinetmaking, engraving, other motor vehicle dealers, and national security and international affairs. But instead of authorizing restricted competition immediately in these four areas, as should be allowed through the statistical study just completed, the SBA placed an additional requirement on any agency wishing to restrict competition to WOSBs to conduct its own internal study proving that it has actively discriminated against women business owners. Not only is this additional layer of study not required or even applicable for gender-based programs, but it represents an additional layer of review even if strict scrutiny were the correct standard to apply in the first place. This additional investigation poses another delay in program implementation and additionally requires the agency to go a step further in making express findings of discrimination against itself. We do not believe that any other groups who are recipients of restricted competition under the Small Business Act, such as 8(a) or service-disabled veterans, are subject to this new "Strict, Strict Scrutiny" as proposed in the rule.

In addition, the creation of this artificial standard at the federal level will have chilling and highly detrimental consequences at the state and local level. One of my volunteer responsibilities is to review the annual WBE performance goal reports issued by our local governments. These programs require proof of availability. Availability cannot be measured accurately until women business owners register their businesses and capabilities. The federal government sets the tone for WOSBs as well. If the federal

government, by actions such as this proposed rule, indicates that WOSBs are not "underrepresented" in federal contracting, the message flows down that WOSBs are not "underrepresented" at any level. And if that is the handwriting on the wall, why should WOSBs attempt to register, particularly where local and state registration requires submission of annual revenues, ownership documents, and tax returns?

Another example is our recent effort to draft and enact new legislation in the State of Kansas which creates a Small and Minority / Women-Owned Business program for the first time. We have thirteen sponsoring organizations and have also just received the endorsement from the Topeka Kansas and Greater Kansas City Chamber of Commerce. If the Chambers, which are largely made up of non-minority businesses, hear that WOSB programs are getting trimmed at the federal level, it is likely their endorsement will be withdrawn at the state and local levels, as well.

We also believe there are some fundamental flaws in the data on which this proposed rule is based. We believe that the RAND study did its best to analyze what SBA directed it to do, but find it insufficient. We believe the Study relies on flawed Nails codes, does not analyze the huge disparity variance between all WOSB awards by contracts versus WOSB CCR awards by contract dollars, and additionally, relies on outdated size standards.

Although the RAND Study concludes that only four NAICS industry codes had been discriminated against, it also expressly admits that collection of accurate data by NAICS code was a problem where: (a) the codes were substantially changed during the study's time frame, thus having some companies listed as one NAICS code at one time, and then transferring to another NAICS code later in the time frame. In other words, the

NAICS code segregation was a constantly moving target during the time frame chosen by the SBA for the study parameters. In addition - and this is a critical point that needs to be addressed here and later - the RAND Study also admits that in the NAICS code review, the SBA did not conduct any independent verification of size standards within that code.

The RAND Study indicates that it followed four primary data gathering processes, each one directed by the SBA and each one predicated solely on attention to WOSBs as prime contractors. Thus, by its control, the SBA prevented the RAND Study from analyzing and recommending its own independent data gathering mechanism which might have ensured a more neutral, and thus more statistically reliable, report. The Study admits: "Discrimination in the awarding of contracts, however, might result from women business owners being less likely to bid on [federal] contracts. This would not be detected if the pool of available firms consists of only firms that have demonstrated their interest by bidding on contracts. Again, the disparity ratio can only measure the difference; it cannot explain it". [6]

We note that in 2006, the SBA amended its size standards to raise the threshold for commercial construction to $13 million for specialty subcontractors and $31 million for general contractors. Despite this fact, the report uses pre-2006 size standards. The correct size standards could easily be located per applicable NAICS codes at: http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&sid=b6e780955530049be4cc0d0a0e391115&rgn=div5&view=text&node=13:1.0.1.1.15&idno=13. See also CFR Section 121.201.

[6] RAND Study, p. 4.

The RAND Study admits it had to rely on outdated NAICS codes. In its footnote (page 8), it states that the Army did not begin reporting transactions above $2500 until FY 2003; the Marine Corps in FY 2004; and most other services and agencies in FY 2005. It is difficult to see how a credible contracting history can be compiled with the absence of the Department of Defense numbers- the largest buyer of federal goods and services in the federal government.

Finally, the Study in Chapter 3, pg. 9, par. 3, noted the difficulty it encountered in gathering data where federal contracts {many using Indefinite Delivery Indefinite Quality (IDIQ) style delivery systems covering both goods and services over several NAICS codes in a single procurement over a 3 year period} makes it difficult or impossible to "parse out" specific NAICS code for actual goods and services purchased, resulting in "generalized" reporting. This and the issue directly above may account for why the disparity methodology using CCR registrations to total contract dollars awarded shows limited disparity. We do not believe the SBA should promulgate a rule which is reliant on insufficient data. Although WIPP believes the rule is seriously flawed and does not need a disparity study, at the very least, we believe the SBA should correct the flaws in the data on which it is basing the proposed program.

In summary, WIPP believes that the SBA proposed rule erroneously relies on a disparity study applying "Strict Scrutiny" instead of "Intermediate Scrutiny" and that the creation of a new "Strict, Strict Scrutiny" standard is unnecessary and lacks parity with other preference programs under the Small Business Act. Furthermore, we believe the proposed rule is based on a study of data which contains flawed data.

We urge the Committee to send SBA back to the drawing board. We urge the Committee to investigate why only 55,000 women-owned businesses are registered in the CCR when in fact, there are 10.4 million women business owners nationwide. Since it has taken the SBA seven years to implement the program, we believe the agency should thoughtfully consider the public comments it gathers through the current 60 day period. WIPP urges Congress to require the SBA to implement a meaningful women's procurement program which will have a positive impact on WOSBs to perform federal contracts.

Thank you for giving me the opportunity to testify. I am happy to answer any questions.